

(d) Gain realized (amount realized \$40,000 less adjusted basis, \$15,000)	\$25,000
(e) Lower of line (c) or line (d)	\$18,000
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(2) Limitation in paragraph (c)(1) of this section:	
(a) Gain recognized (determined without regard to section 1255)	\$8,000
(b) Minus: Gain recognized as ordinary income under section 1251(c)(1)	\$5,000
(c) Difference	\$3,000
(3) Lower of line (1)(e) or line (2)(c)	\$3,000

Thus, the entire gain recognized under section 351(b) (determined without regard to sections 1251 and 1255), \$8,000, is recognized as ordinary income since that amount is equal to the sum of the gain recognized as ordinary income under section 1251(c)(1), \$5,000, and under section 1255(a)(1), \$3,000.

(d) *Treatment of section 126 property received by a transferee in a disposition by gift and certain tax-free transactions—(1) General rule.* If section 126 property is disposed of in a transaction which is either a gift to which paragraph (a)(1) of this section applies, or a completely tax-free transfer to which paragraph (c)(1) of this section applies, then for purposes of section 1255—

(i) The aggregate of the excludable portions under section 126 in respect of the land in the hands of the transferee immediately after the disposition shall be an amount equal to the amount of such aggregate in the hands of the transferor immediately before the disposition, and

(ii) For purposes of applying section 1255 upon a subsequent disposition by the transferee (including a computation of the applicable percentage), the dates of receipt of section 126 payments shall not be affected by the dispositions.

(2) *Certain partially tax-free transfers.* If section 126 property is disposed of in a transaction which either is in part a sale or exchange and in part a gift to which paragraph (a)(2) of this section applies, or is a partially tax-free transfer to which paragraph (c)(1) of this section applies, then for purposes of section 1255 the amount determined under paragraph (d)(1) of this section shall be reduced by the amount of gain taken into account under section 1255 by the transferor upon the disposition. Upon a subsequent disposition by the transferee, the dates of receipt of section 126 payments remain the same in the hands of the transferee as they were in the hands of the transferor.

With respect to the 175 and 182 deductions taken by the transferee, the holding period shall not include the holding period of the transferor.

(3) *Examples.* The provisions of this paragraph may be illustrated by the following examples:

Example (1). Assume the same facts as in example (1) of paragraph (a)(4) of this section. Therefore, on the date B receives the land in the gift transaction, under paragraph (d)(1) of this section the aggregate of excludable portions under section 126 in respect of the land in the hands of B is the amount in the hands of A, \$24,000, and for purposes of applying section 1255 upon a subsequent disposition by B (including a computation of the applicable percentage) the date the section 126 payments were received is the same as it was when the property was in A's hands (January 15, 1981).

Example (2). Assume the same facts as in example (2) of paragraph (a)(4) of this section. Under paragraph (d)(2) of this section, the aggregate of excludable portions under section 126 which pass over to B for purposes of section 1255 is \$14,000 (\$24,000 excluded under section 126 minus \$10,000 gain recognized under section 1255(d)(1) in accordance with example (2) of paragraph (a)(4) of this section). The date the section 126 payments were received is the same as when the property was in B's hands (January 15, 1981).

(e) *Disposition of section 126 property not specifically covered.* If section 126 property is disposed of in a transaction not specifically covered under §16A.1255-1, and this section, then the principles of section 1245 shall apply.

PART 17—TEMPORARY INCOME TAX REGULATIONS UNDER 26 U.S.C. 103(c)

AUTHORITY: Sec. 7805 of the Internal Revenue Code of 1954; 68A Stat. 917 (26 U.S.C. 7805).

§17.1 Industrial development bonds used to provide solid waste disposal facilities; temporary rules.

(a) *In general.* Section 103(c)(4)(E) provides that section 103(c)(1) shall not apply to obligations issued by a State or local governmental unit which are part of an issue substantially all the proceeds of which are used to provide solid waste disposal facilities. Section 1.103-8(f) of this chapter provides general rules with respect to such facilities and defines such facilities. In the

case of property which has both a solid waste disposal function and a function other than the disposal of solid waste, only the portion of the cost of the property allocable to the function of solid waste disposal (as determined under paragraph (b) of this section) is taken into account as an expenditure to provide solid waste disposal facilities. A facility which otherwise qualifies as a solid waste disposal facility will not be treated as having a function other than solid waste disposal merely because material or heat which has utility or value is recovered or results from the disposal process. Where materials or heat are recovered, the waste disposal function includes the processing of such materials or heat which occurs in order to put them into the form in which the materials or heat are in fact sold or used, but does not include further processing which converts the materials or heat into other products.

(b) *Allocation.* The portion of the cost of property allocable to solid waste disposal is determined by allocating the cost of such property between the property's solid waste disposal function and any other functions by any method which, with reference to all the facts and circumstances with respect to such property, reasonably reflects a separation of costs for each function of the property.

(c) *Example.* The principles of this paragraph may be illustrated by the following example:

Example. Company A intends to construct a new facility to process solid waste which City X will deliver to the facility. City X will pay a disposal fee for each ton of solid waste that City X dumps at the facility. The waste will be processed by A in a manner which separates metals, glass, and similar materials. As separated, some of such items are commercially saleable; but A does not intend to sell the metals and glass until the metals are further separated, sorted, sized, and cleaned and the glass is pulverized. The metals and pulverized glass will then be sold to commercial users. The waste disposal function includes such processing of the metals and glass, but no further processing is included.

The remaining waste will be burned in an incinerator. Gases generated by the incinerator will be cleaned by use of an electrostatic precipitator. To re-

duce the size and cost of the electrostatic precipitator, the incinerator exhaust gases will be cooled and reduced in volume by means of a heat exchange process using boilers. The precipitator is functionally related and subordinate to disposal of the waste residue and is therefore property used in solid waste disposal. The heat can be used by A to produce steam. Company B operates an adjacent electric generating facility and B can use steam to power its turbine-generator. B needs steam with certain physical characteristics and as a result A's boilers, heat exchanger and related equipment are somewhat more costly than might be required to produce steam for some other uses. The disposal function includes the equipment actually used to put the heat into the form in which it is sold.

Company A intends to construct pipes to carry the steam from A's boiler to B's facility. When converted to such steam the heat is in the form in which sold, and therefore the disposal function does not include subsequent transporting of the steam by pipes. Similarly, if A installed generating equipment and used the steam to generate electricity, the disposal function would not include the generating equipment, since such equipment transforms the commercially saleable steam into another form of energy.

[T.D. 7362, 40 FR 26028, June 20, 1975]

PART 18—TEMPORARY INCOME TAX REGULATIONS UNDER THE SUBCHAPTER S REVISION ACT OF 1982

Sec.

18.0 Effective date of temporary regulations under the Subchapter S Revision Act of 1982.

18.1371-1 Election to treat distributions as dividends during certain post-termination transition periods.

18.1379-1 Transitional rules on enactment.

18.1379-2 Special rules for all elections, consents, and refusals.

AUTHORITY: 26 U.S.C. 7805.

SOURCE: T.D. 7872, 48 FR 3590, Jan. 26, 1983, unless otherwise noted.